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NEWS RELEASE

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FOR RELEASE

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Auditor of State David A. Vaudt today released a report on the Iowa Lottery Authority (Iowa Lottery) for the period July 1, 2002 through June 30, 2010. The review was conducted to determine the impact of the Iowa Lottery becoming an Authority.

From 1985 to 2003, the Iowa Lottery operated as a State agency and was subject to rules and regulations consistent with all other state agencies. However, effective September 1, 2003, the Legislature established the Iowa Lottery Authority. As an Authority, the Iowa Lottery is not subject to general state government oversight applicable to state agencies.

Vaudt reported annual revenues have increased since fiscal year 2004, when the Iowa Lottery became an Authority. However, Vaudt concluded the increased revenues realized by the Iowa Lottery were not a result of the Iowa Lottery becoming an Authority. All the activities which resulted in increased revenues could have been conducted by the Iowa Lottery as a state agency. Although certain revenue-generating activities may have been implemented more quickly due to the Iowa Lottery's status as an Authority, each of the activities resulting in significant revenues was permissible for the Iowa Lottery to conduct as a state agency. In addition, other state lotteries which operated as state agencies for the same time period realized similar revenue increases.

Vaudt reported the Iowa Lottery's status as an Authority has also allowed the Iowa Lottery to make significant changes to its compensation practices for certain employees. In accordance with the *Code of Iowa*, the Iowa Lottery's Chief Executive Officer (CEO), with approval from the Iowa Lottery Board, has power to designate particular employees as "key personnel." Of the key personnel, the CEO is appointed by the Governor and compensation and employment terms for the CEO are set by the Governor. Other key personnel are exempt from the State's classification and pay plans and their salaries are set by the Iowa Lottery.

Vaudt reported:

- As a result of the Iowa Lottery becoming an Authority, the Legislature no longer establishes a salary range for the Iowa Lottery CEO, as it does for other Department Directors. During the 6 years from fiscal year 2005 through fiscal year 2010, Governor Vilsack and Governor Culver authorized annual salary increases for the prior and current Iowa Lottery CEOs which totaled \$358,856.43 more than would have been possible if the Legislative salary range for the Iowa Lottery CEO had been maintained. The Iowa Lottery has increased the

salaries of other key personnel to amounts significantly higher than the maximum salary amounts they would have been eligible to receive if the Iowa Lottery had remained a state agency. Vaudt reported the increased annual authorized salaries of the other 8 key personnel totaled \$589,429.23 more than would have been possible if the State's salary ranges for the 8 positions had been maintained during the 6 years from fiscal year 2005 through fiscal year 2010.

- The Iowa Lottery hired a consulting firm to conduct a compensation review in 2004 after the Iowa Lottery became an Authority. However, Vaudt determined the compensation review was conducted in a manner which virtually guaranteed Iowa Lottery salaries would appear low. The compensation review primarily utilized private sector and nonprofit entities as the basis of its market salary comparison for each key position included in the review. In addition, the review was limited to salary data from only 7 state lotteries. According to an article published in 2009, all 7 CEO's of each of the state lotteries utilized for the compensation review were among the highest paid state lottery CEO's in the country. According to the consultant, when the compensation review began in 2004, the prior Iowa Lottery CEO directed the consultant to limit the comparison with other lotteries to the 7 state lotteries with entrepreneurial structures and to exclude all the other state lotteries from the review.

After receiving the results of the compensation review, the Iowa Lottery approved increasing a majority of the key personnel salaries to the maximum salary amount recommended in the compensation review over a 2-year period. However, according to the consultant, she recommended a large salary range to allow for gradual salary growth over time. The consultant stated she did not recommend increasing key personnel salaries to the maximum salary included in the compensation review and it was not a practice she would have supported had she been aware of how the Iowa Lottery would implement the results of the review. After completion of the compensation review, all Iowa Lottery key personnel received significant salary increases.

- Governor Vilsack and Governor Culver approved incremental salary increases for the prior Iowa Lottery CEO from \$122,811.38 in fiscal year 2003 to \$239,777.46 (a 95% increase) in fiscal year 2008, when he retired. In addition, when the prior Iowa Lottery CEO retired, he began receiving significantly higher IPERS benefits for the duration of his life because of the salary increases he received when the Iowa Lottery became an Authority. According to IPERS, the prior Iowa Lottery CEO's IPERS benefits are nearly 60% higher than the IPERS benefits he would have received had the Iowa Lottery remained a state agency.
- From fiscal year 2005 to fiscal year 2010, the total salaries approved for the Iowa Lottery CEO and key personnel in excess of the State's pay plan totaled \$948,285.66. The additional IPERS and payroll contributions associated with those approved salaries total \$87,175.32. Accordingly, since becoming an Authority, the authorized salaries in excess of

the maximum allowable under the State's pay plan for the Iowa Lottery CEO and key personnel plus the related payroll contributions is over \$1 million.

- The Iowa Lottery Board inappropriately delegated the compensation review to Lottery officials who would be financially impacted by the results of the review. The delegation created several issues with critical parameters of the compensation review, which caused flawed compensation review results and inadequately justified key personnel salaries. It appears the Iowa Lottery Board failed to properly exercise its fiduciary responsibilities in determining and approving appropriate key personnel salaries.
- Iowa Lottery key personnel received significantly larger salary increases and larger overall salaries than their counterparts in other State entities. By comparing the Iowa Lottery CEO's base salary to comparable positions at other larger State entities, it is readily apparent the Iowa Lottery outpaced other State entities in regard to CEO pay increases and total base pay. Other Iowa Lottery key personnel also received higher salaries than their counterparts at larger State entities.

In addition, a majority of State Department Directors included in the review did not receive any salary increases in fiscal years 2004 and 2005 while Iowa Lottery salaries increased substantially. A majority of the State Division Directors included in the review recognized salary increases ranging from 6.12% to 13.38%. During this two-year period, the prior Iowa Lottery CEO's salary increased 68.55% and other key personnel received salary increases ranging from 13.86% to 27.55%.

- Some Iowa Lottery personnel receive more compensation than allowed for their counterparts in State entities even though the Iowa Lottery has continued to operate in essentially the same manner as was done prior to becoming an Authority. Making the Iowa Lottery an Authority has given the Iowa Lottery CEO and Board the flexibility to reward employees beyond restrictions placed on other State entities. As a result, there is an appearance Iowa Lottery officials are more valuable than other State employees.

Vaudt also reported a published article showed the current Iowa Lottery CEO's salary for 2009 to be the 9th highest of 44 Lotteries reviewed. The 2008 salary of the prior Iowa Lottery CEO would have been 5th highest of those 44 Lotteries.

While the Iowa Lottery CEO's salary is one of the highest in the country, the amount of funds transferred to the State's General Fund as a percentage of ticket sales is one of the lowest. According to certain U.S. Census data for fiscal year 2007, the Iowa Lottery's sales per capita were 58.5% lower than the national average and administrative costs were 10.2% higher than the national average.

Based on the results of the review, Vaudt recommended:

- The Legislature establish controls over compensation practices of all State Authorities, including the Iowa Lottery, to ensure Authority status does not result in salaries which

are not based on employee responsibilities, experience and other valid documented considerations. In addition, the Legislature, which authorized key personnel positions in the Iowa Lottery's enabling legislation, should determine if it is necessary to maintain key positions.

- The Legislature conduct a comparison of all State Authority personnel salaries with State agency personnel salaries to identify any other salary anomalies.
- The Iowa Lottery Board work with the Department of Administrative Services to conduct an independent compensation review, including State personnel operating in similar positions as well as state lotteries with comparable state populations, demographics and revenues. The independent compensation review should include consideration of cost of living and employee benefits.
- The Iowa Lottery CEO and Board review current key personnel salaries at the Iowa Lottery to determine whether they are appropriate after the Board's independent compensation review is completed.

A copy of the report is available for review in the Office of Auditor of State and on the Auditor of State's web site at <http://auditor.iowa.gov/specials/1160-6270-B0P0.pdf>.

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